Abstract: As a result of the current estate tax exemption amount ($12.92 million in 2023), many people are no longer concerned with federal estate tax. This article points out that before 2011, a much smaller dollar amount resulted in many people attempting to avoid estate tax. Now, because many estates won't be subject to estate tax, more planning can be devoted to saving *income taxes* for heirs. A sidebar briefly looks at certain exclusions or discounts.

Your estate plan: Don't forget about income tax planning

As a result of the current estate tax exemption amount ($12.92 million in 2023), fewer people are concerned with federal estate tax. Before 2011, a much smaller dollar amount resulted in many people scrambling to avoid estate tax. Now, because many estates won't be subject to estate tax, more planning can be devoted to saving *income taxes* for your heirs.

Note: The federal estate tax exclusion amount is scheduled to sunset after 2025. Beginning in 2026, the amount is due to be reduced to $5 million, adjusted for inflation, unless Congress acts to extend the higher amount or institute a new amount.

In light of the current large exemption amount, here are some strategies to consider:

Gifts that use the annual exclusion

One benefit of using the gift tax annual exclusion to make transfers during life is to save estate tax. This is because both the transferred assets and any post-transfer appreciation generated by those assets are removed from the donor's estate.

Estate tax savings may not be an issue because of the large estate exemption amount. Further, making an annual exclusion transfer of appreciated property carries a potential income tax cost because the recipient receives the donor's basis upon transfer. If the heir sells the gifted property, it could trigger capital gains tax that could be significant. If there's no concern that an estate will be subject to estate tax, even if the gifted property grows in value, then the decision to make a gift should be based on other factors.

Let's say that a gift is made to help a relative buy a home. Depending on the circumstances, using appreciated property to make the gift may not be prudent from a tax perspective. Instead, if the appreciated property is held until the donor's death, under current law, the heir recipient would get a step-up in basis that would wipe out the capital gains tax.

Spouse's estate

Years ago, spouses often undertook complicated strategies to equalize their estates so that each could take advantage of the estate tax exemption amount, perhaps with a two-trust plan. "Portability," or the ability to apply the decedent's unused exclusion amount to the surviving spouse's transfers during life and at death, became effective for estates of decedents that died after 2010. If elected, portability allows the surviving spouse to apply the unused portion of a decedent’s applicable exclusion amount (the deceased spousal unused exclusion amount) as calculated in the year of the decedent’s death. This gives married couples more flexibility in deciding how to use their exclusion amounts. Bear in mind, though, that portability is a federal estate tax concept. Generally, those states that impose an estate tax don’t recognize portability. Thus, if you may be subject to estate tax at the state level you should be sure to plan accordingly.

Contact us to discuss these strategies and how they relate to your estate plan.

Sidebar: Estate exclusions or valuation discounts: Still good strategies?

Some estate exclusion or valuation discount strategies to avoid inclusion of property in an estate may no longer be worth pursuing. For example, the special use valuation of qualified real property in a business based on the property’s actual use, rather than the highest and best use, may save only a small amount of estate tax. You may achieve a better estate tax outcome by having the property included in the estate or not qualify for valuation discounts so that the property receives a step-up in basis.